

1
DBKBBITH Hearing
1 UNITED STATES DISTRICT COURT
1 SOUTHERN DISTRICT OF NEW YORK
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3 BITVESTMENT PARTNERS LLC,
3
4 Plaintiff,
4
5 v. 13 CV 7632 (RWS)
5
6 COINLAB, INC., CLI HOLDINGS,
6 INC., ALYDIAN INC., PETER
7 VESSENES and JOHN DOE,
7
8 Defendants.
8
9 -----x
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10 New York, N.Y.
10 November 20, 2013
10 3:06 p.m.
11
11 Before:
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12 HON. ROBERT W. SWEET,
13
13 District Judge
14
14 APPEARANCES
15
15 REYHANI NEMIROVSKY LLP
16 Attorneys for Plaintiff
16 BRYAN ISAAC REYHANI
17
17 LOEB & LOEB LLP
18 Attorneys for Plaintiff
18 DANIELLE JANINE KIWAK
19
19 NESENOFF & MILTENBERG, LLP
20 Attorneys for Defendants
20 MARCO AURELIO SANTORI
21
21 BRESKIN JOHNSON TOWNSEND PLLC
22 Attorneys for Defendants
22 ROGER M. TOWNSEND
23
24
25
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DBKBBITH Hearing

1 MR. TOWNSEND: Thank you.

2 DANIEL H. GALLANCY,

3 called as a witness by the Defendants,

4 having been duly sworn, testified as follows:

5 THE DEPUTY CLERK: Please state your full name and

6 spell your first name and last name slowly for the record.

7 THE WITNESS: Daniel H. Gallancy. D-a-n-i-e-l middle
8 initial H, G-a-l-l-a-n-c-y.

9 THE DEPUTY CLERK: Thank you, Mr. Gallancy. Please be
10 seated.

11 DIRECT EXAMINATION

12 BY MR. TOWNSEND:

13 Q. Good afternoon, Mr. Gallancy. I'm sorry, it sounds like
14 I'm mispronouncing your name. It's Gallancy. Is that
15 correct?

16 A. Yes, that's correct.

17 Q. And you're a chartered financial analyst. Is that right?

18 A. That's correct.

19 Q. And what training did you receive to become a CFA?

20 A. I passed a series of exams and satisfied a series of work
21 requirements.

22 Q. And that's how long a process?

23 A. The exams take approximately three years. There are ways
24 to do it a little bit faster, but approximately three years.

25 Q. And you took three years to do it?

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- 1 A. Yes, sir.
2 Q. And in your capacity as a CFA, you have knowledge of
3 complex financial models. Is that right?
4 A. I have knowledge of financial models.
5 Q. Okay.
6 A. Complexity is a matter of subjectivity.
7 Q. Sure. But you regularly construct financial models. Is
8 that right?
9 A. I have in the past regularly constructed financial models,
10 yes, sir.
11 Q. And usually, in your experience in constructing financial
12 models, most businesses have overhead. Is that right?
13 A. Yes, sir.
14 Q. And in the contract that you entered into with CoinLab and
15 Alydian, that contemplated that you would be paid bitcoins
16 mined by CoinLab. Is that right?
17 A. I'm sorry?
18 Q. In the contract that you entered into with CoinLab and
19 Alydian, that contemplated that you would be delivered bitcoins
20 that were mined by CoinLab or Alydian. Is that right?
21 A. The contract said I was to receive 100 percent of CoinLab
22 and Alydian and CLI Holdings' mining output, with the exception
23 of that which is to go to Crystal Island were they to
24 participate in the deal, and operating and capital expenditures
25 as approved by all parties.

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1 Q. Correct.

2 And so it was contemplated at that time that the net
3 of bitcoins would be less payments to Crystal Island. Right?

4 A. That's correct.

5 Q. And net payments for capital and operational expenditures.
6 Correct?

7 A. Not necessarily.

8 Q. Okay. Why not necessarily?

9 A. The project, if fully capitalized, needn't use mining
10 output for capital expenditures but, rather, would use the
11 input capital for capital expenditures and operating expenses.

12 Q. And upon what basis do you believe that outside money would
13 fund capital and operational expenditures?

14 A. On the basis of discussions with the defendant.

15 Q. Who specifically?

16 A. Peter Vessenes and the rest of the CoinLab team.

17 Q. And they told you that they would just absorb all of the
18 operational and capital expenditures?

19 A. We had discussed various different scenarios, amongst them
20 the usage of input capital for operating and capital
21 expenditures. And also amongst them the usage of mining output
22 for capital and operating expenditures. The primary source of
23 capital expenditures was to be the input capital.

24 Q. Okay. But certainly it was contemplated that at least a
25 portion, you'll acknowledge --

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- 1 A. I will not acknowledge. That's not the case.
2 Q. Well, isn't that what you just said?
3 A. I said under certain circumstances. We had contemplated
4 several different deal structures.
5 Q. And you believed you had a veto right for any capital and
6 operational expenditures. Correct?
7 A. I have a veto right for any capital and operational
8 expenditures which I did not intend to use unless the defendant
9 made it such that I had to.
10 Q. And you did use it. Correct?
11 A. I attempted to use it.
12 Q. Okay.
13 A. Although without any real success.
14 Q. Okay. And you would acknowledge that the veto right for
15 capital and operational expenditures was also a right that all
16 parties had. Right?
17 A. Yes.
18 Q. All right.
19 A. That's true. For mining output, that is correct.
20 Q. So CoinLab could elect not to spend capital and operational
21 expenditures for mining output. Correct?
22 A. CoinLab could elect not to use the funds from its mining
23 output to fund capital or operating expenditures as long as it
24 fulfilled its requirements to -- if Crystal Island were to
25 invest -- Crystal Island and as long as it were to fulfill its

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- 1 operations to Bitvestment.
2 Q. Well, it doesn't say that, does it?
3 A. It does say that.
4 Q. It says that they only have a veto right provided they paid
5 you first?
6 A. The language in the contract says that CoinLab will provide
7 100 percent of mining output until such time that Bitvestment
8 receives 7,984-some-odd bitcoins with the exception of mining
9 output that would go to Crystal Island or capital and operating
10 expenditures as approved by all parties.
11 Q. Okay.
12 A. To be clear.
13 Q. And so, therefore, if CoinLab doesn't approve the capital
14 and operational expenditures, it won't get spent. Correct?
15 A. Well, the first part of the sentence says "CoinLab is to
16 provide 100 percent of mining output until Bitvestment receives
17 7,984 bitcoins."
18 Q. So when it says the veto right applies to all parties,
19 what you're really saying it is only applies to you. Is that
20 right?
21 A. No, I'm saying that the veto right would only be-- that's
22 incorrect.
23 Q. Okay.
24 A. To be clear --
25 Q. They have the right to the same under the contract.

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1 Correct?

2 A. Fair enough.

3 Q. It applies to all parties equally. Correct?

4 MR. REYHANI: Objection. Asked and answered like
5 three times already.

6 THE COURT: Overruled.

7 MR. TOWNSEND: Well, the answer keeps changing, so I
8 just want to make clear.

9 Q. Each party has a right not to spend the capital and
10 operational expenditures. Correct?

11 A. I suppose.

12 Q. Thank you.

13 And if they don't expend capital and operational
14 expenditures, then necessarily they're not going to mine
15 bitcoins. Right?

16 A. No, absolutely not correct.

17 Q. And why is that?

18 A. Because if the project is capitalized in the first place as
19 contemplated, and as it was, the input capital would be
20 sufficient to cover capital and operating expenditures. That's
21 the whole point.

22 Q. In your capacity as a CFA, do you recommend that people
23 engage in businesses that lose money?

24 A. I don't make recommendations that people engage in
25 businesses one way or the other in my capacity as a CFA. I

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- 1 analyze companies.
2 Q. Okay. And you analyzed this company, Alydian. Correct?
3 A. Correct.
4 Q. You did a detailed financial model of Alydian, did you
5 not?
6 A. I did a detailed financial model that would be for this--
7 that would be for a mining project for Alydian and/or CoinLab
8 and/or CLI Holdings.
9 Q. Okay. So that's a yes. Right?
10 A. I just answered your question, sir.
11 Q. So you did a detailed financial analysis of the proposed
12 mining operation that was being run by Hans Olsen and Peter
13 Vessenes and the companies that they work for. Is that
14 right?
15 A. Among other participants, yes.
16 Q. Okay. And you didn't produce that financial analysis, did
17 you?
18 A. Produce it?
19 Q. In this litigation.
20 A. I didn't present a copy of it, no. I presented it to
21 Crystal Island, to Cedar Hill.
22 Q. But you haven't provided it to the Court or in this
23 litigation?
24 A. It was not requested.
25 Q. Okay. But you didn't use it-- you have the burden of proof
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1 in this litigation. Right? Okay.

2 You would agree that bitcoins are an inherently risky
3 and speculative investment, would you not?

4 A. I would agree that bitcoins possess significant risks,
5 yes.

6 Q. And you would further agree that bitcoin mining is a risky
7 and unproven investment. Is that right?

8 A. I would agree that bitcoin mining has its risks. It's not
9 unproven insofar as whether or not it is achievable. It is
10 certainly achievable.

11 Q. Is it achievable with a positive cash flow?

12 A. Depending on its execution, yes.

13 Q. Okay. And you didn't provide any evidence of any positive
14 financial models that shows any bitcoin operation that
15 generates a positive cash flow, did you?

16 A. I did, indeed, provide that sort of model to Crystal
17 Island, Cedar Hill, and they, indeed, upon that model were
18 willing to invest.

19 Q. Okay. But you didn't provide it in support of your motion
20 for preliminary injunction, did you?

21 A. I didn't provide it in this particular case, no. I
22 provided it in the past to those who were interested in the
23 investment.

24 Q. So you don't have any evidence to present now or in any way
25 in this proceeding that supports that --

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- 1 A. I don't have my laptop computer with me, no, sir.
2 Q. And you recommended to Cedar Hill-- first of all, who is
3 Cedar Hill?
4 A. It's an investment fund.
5 Q. Okay. And what's your relationship with Cedar Hill?
6 A. Its principals are people with whom I'm friendly.
7 Q. Okay. And who is Crystal Island?
8 A. Crystal Island is a subsidiary of Cedar Hill.
9 Q. Okay. And then at some point they engaged you to do
10 financial planning. Is that right?
11 A. They did not engage me to do financial planning. They
12 engaged me to assist them with the diligence of this deal.
13 Q. Okay. And did they pay you for that?
14 A. No, they did not.
15 Q. And why did you do --
16 A. There was an offer of compensation subsequent to the deal
17 if it were-- if they were to go through with it.
18 Q. Okay. And what was that compensation?
19 A. We were actually still in the middle of negotiating it. So
20 there was not a final specific amount, but it was likely to be
21 5 percent of the profits from the deal.
22 Q. Okay. So that was a profit-based deal?
23 A. Correct. So obviously I thought it would be profitable.
24 Q. Right.
25

You also testified in your declaration that you

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1 thought that the project was grossly mismanaged. Is that
2 right?

3 A. The project, prior to the arrival of Hans, I believe was in
4 the past grossly mismanaged.

5 Q. Okay. But you put in your declaration that the project was
6 grossly mismanaged, right?

7 MR. REYHANI: Objection. Asked and answered.

8 THE COURT: Overruled.

9 Q. You can answer.

10 A. Yes, I believe that the project was in the past grossly
11 mismanaged. That's correct.

12 Q. Okay. And despite the gross mismanagement, you recommended
13 to Crystal Island and Cedar Hill that they invest money. Is
14 that right?

15 A. Because it was essentially under new management.

16 Q. Right. But you specifically stated in your declaration
17 that it was Mr. Vessenes that was responsible for the gross
18 mismanagement. Right?

19 A. Yes. And, thankfully, Mr. Olsen came along and did his
20 best to save the day.

21 Q. Right. But they went into bankruptcy, didn't they?

22 MR. REYHANI: Who's "they"?

23 Q. Alydian went into bankruptcy. Correct?

24 MR. TOWNSEND: Thank you.

25 A. So, yes, Alydian did indeed go into bankruptcy, but I don't

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1 believe that's because it had negative cash flow.

2 Q. And upon what basis do you allege that?

3 A. Well, I don't have all of the data from Alydian.

4 Q. Thank you. That's --

5 A. But your --

6 Q. That's enough.

7 A. But your colleague made it clear to me he was going to file
8 for bankruptcy if I pursued this litigation.

9 Q. Well, you don't know the financial model of Alydian, do
10 you?

11 A. I created one several months ago for Cedar Hill.

12 Q. Right.

13 A. I don't have their internal-- I do not have CoinLab's
14 internal model, no. I have an older version of it. I do not
15 have a current version of it.

16 Q. So you have no idea what happened between August of 2013
17 and the time they filed for bankruptcy. Is that right?

18 A. I don't have a full and complete picture of that, no. I do
19 know that the price of bitcoin has increased.

20 Q. You also know that the speed of the bitcoin network has
21 increased exponentially as well. Is that right?

22 A. As was contemplated in the original model.

23 Q. But it's increased at a much faster rate that was
24 contemplated in the original model. Right?

25 A. No, we had various different-- well, hold on. Whose model?

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1 Vessenenes's model or my model?

2 Q. No one's seen your model, so we don't know about your
3 model. So we have to talk about Alydian's model

4 A. So I don't remember the details of Alydian's model
5 specifically. I do know that in my model, and in my model in
6 discussions with Cedar Hill, we had contemplated various rates
7 of increase in speed, as high as and, in fact, in crazy cases,
8 far higher than that which has actually occurred.

9 Q. Okay. Well, Mr. Vessenenes and Mr. Olsen can talk about what
10 actually occurred based on the reality of the situation.

11 You agree in the agreement to bear all the risk from
12 any changes in future laws, regulations, changes in technology
13 and other forces not within CoinLab's control. Is that
14 right?

15 A. That, indeed, I believe is the text of the agreement, but I
16 don't have it in front of me. If you say it is, then I believe
17 so.

18 Q. And would a change in the state of the art of chip
19 technology be a change in technology?

20 A. Definitely not.

21 Q. Definitely not?

22 A. Definitely not.

23 Q. And why is that? Is a chip a technology?

24 A. A chip is a piece of silicon which has a purpose in terms
25 of its input and output.

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- 1 Q. Okay. And how is that different from a technology?
2 A. I'm not really sure how to answer that question.
3 Q. I think you did.
4 A. It's not, though. The answer is no.
5 Q. Okay. Chips are not technology. I understand --
6 A. No, chips are chips. Technology -- actually, if you want
7 to look at it from a semantic basis, technology refers to a
8 broader category of items.
9 Q. Okay. Would a semiconductor be a technology?
10 A. Technology-- I don't have a dictionary definition of
11 technology in front of me.
12 Q. Would a computer be a technology?
13 A. These are examples of technological innovations.
14 Q. Okay. So the chip is a technological innovation. Is that
15 right?
16 A. A chip is one example of a technological innovation.
17 Q. Okay. And a new chip would be a new example of a new
18 technological innovation. Is that right?
19 A. That's a fair statement, yes.
20 Q. And then, also, you agreed in the same disclaimer of
21 warranties that you understand and agree that services and
22 bitcoins are the result of relatively new technologies and
23 market exchanges. Is that right?
24 A. The technologies in that paragraph don't refer to --
25 Q. Well, I'm actually going to change your focus to the

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1 "market exchanges" language. So moving on --

2 A. So I don't know exactly what the words "market exchanges"
3 in that context means. If he's referring to-- if the
4 contract-- if that means are there new bitcoin exchanges,
5 there are new exchanges that will trade fiat currency for
6 bitcoins.

7 MR. TOWNSEND: May I approach, your Honor?

8 THE COURT: Sure.

9 Q. I'm going to hand you that and I'll ask you to look at it.
10 I'd draw your attention to Tab 2.

11 A. Yes, sir.

12 Q. Do you recognize this document?

13 A. I do, indeed.

14 Q. What is this?

15 A. This is the contract that I signed --

16 Q. You're on Tab 1, I think.

17 A. My apologies. Tab 2 is not a contract.

18 Q. No, it's not, your Honor-- I mean, no, it's not,
19 Mr. Gallancy. It's an e-mail from you. Is that right?

20 A. Indeed, it is.

21 Q. It's an e-mail that you sent on November 12th. Is that
22 right?

23 A. Yes, it is.

24 Q. And in it you're lauding a bitcoin exchange. Is that
25 right?

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- 1 A. I am, indeed.
2 Q. And that bitcoin is called-- exchange is called ItBit. Is
3 that right?
4 A. It is, correct.
5 Q. And there are other coin exchanges, aren't there?
6 A. There are, indeed.
7 Q. Bitstamp.net is a bitcoin exchange?
8 A. Correct.
9 Q. BTC-e.com is a bitcoin exchange?
10 A. I believe so, yes. I haven't used that one.
11 Q. And Mt.Gox.com is a bitcoin exchange. Is that right?
12 A. Yes.
13 Q. Which bitcoin exchange do you use?
14 A. I've used several bitcoin exchanges.
15 Q. Okay. And how do they work?
16 A. I don't understand.
17 Q. How does a bitcoin exchange work? How do you get a
18 bitcoin?
19 A. The bitcoin exchange, it usually involves going to a
20 website, and the underpinnings of that website are a matching
21 engine that matches buy orders and sell orders.
22 Q. Okay.
23 A. Sort of like a-- I don't know what it's like. It's a
24 matching one.
25 Q. Is it like a stock exchange?

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- 1 A. It's not really the same as a stock exchange. A stock
2 exchange-- a bitcoin exchange tends to be an amalgamation of
3 several different items that all get compressed into one thing.
4 A stock exchange is a discrete entity, like the New York Stock
5 Exchange, and then you'd have brokers going to that entity and
6 various intermediaries. So it's not quite analogous to a stock
7 exchange although it bears some similarities to it.
8 Q. But as a consumer you would pay dollars or other
9 traditional fiat-based currency and in exchange you would
10 receive bitcoins. Right?
11 A. That's one way you would do it.
12 Q. Okay. And, also, if you sold bitcoins, on those exchanges
13 you could sell a bitcoin and receive a dollar or a euro or a
14 yen or another foreign currency. Is that right?
15 A. Yes. All of this presupposes that the technology that
16 underlies bitcoins doesn't crash in the midst of this.
17 Q. Correct.
18 A. Which has happened.
19 Q. But you've used them before successfully and turned them
20 into dollars. Right?
21 A. I've used them before both successfully and unsuccessfully.
22 Q. But today if you had eight thousand bitcoins, you could
23 sell them for dollars. Is that right?
24 A. I don't know that. I probably could, but it's not certain.
25 But, yes, I probably could.

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- 1 Q. Okay. And, in fact, in your declaration, you identify
2 bitcoins as a currency. Correct?
3 A. I don't have a copy of my declaration in front of me.
4 Q. In fact, you do.
5 A. Okay. Tell me what tab to look at, please.
6 Q. Turn yourself to the next tab, Tab 3.
7 A. I do.
8 Q. Okay. If you look at paragraph 5, you testify that
9 bitcoins are a virtual currency. Is that right?
10 A. "Maintained through internet pier-to-pier network." The
11 tail half of that sentence is essential.
12 Q. Okay. But you also --
13 A. Without the tail half of the sentence, the first half
14 wouldn't be correct.
15 Q. Okay. But it's a medium of exchange in which you can turn
16 dollars into bitcoins. That's how the exchange --
17 A. Wait. An exchange is or a bitcoin is?
18 Q. Well, a bitcoin can be turned into dollars. Right? We've
19 already established that. But a bitcoin is a virtual currency.
20 Right?
21 A. We haven't established that. You can at times exchange
22 bitcoins for dollars. That is not necessarily the case at all
23 times and is not necessarily the case in the future.
24 Q. It's probably the case today. Right?
25 A. It's probably the case today, yes.

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- 1 Q. And, in fact, you testified or you provided testimony from
2 the director of FinCEN-- first of all, what is FinCEN?
3 A. FinCEN is an arm of the treasury department.
4 Q. And FinCEN has engaged in regulation of bitcoins. Correct?
5 A. So FinCEN -- from what I understand, I'm not a lawyer --
6 has provided guidance regarding the way bitcoin is to be
7 treated. I'm not intimately familiar with everything that
8 FinCEN has done in the bitcoin ecosystem. I have read the
9 March 2013 guidance. I don't have it with me.
10 Q. And you've also read the November 18th, 2013 testimony from
11 FinCEN as well. Correct?
12 A. I've read portions of it, yes.
13 Q. Okay. And you cite to it in your second declaration you
14 filed yesterday. Is that right?
15 A. That's correct.
16 Q. Okay. And if I draw your attention to the next tab, Tab 4,
17 paragraph 47, on page 15.
18 A. Yes, sir.
19 Q. And in that you say that the director of FinCEN testified
20 that "virtual currency is a medium of exchange that operates
21 like a currency in some environments but does not have all the
22 attributes of real currency.... And since a convertible virtual
23 currency either has an equivalent value in real currency, or
24 acts as a substitute for real currency, it qualifies as 'other
25 value that substitutes for currency' under the definition of

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1 'money transmission services.'" Is that right?

2 A. That is, indeed, in the declaration, yes, sir.

3 Q. Okay. And so it's your understanding the Department of
4 Treasury treats the exchange of bitcoins as a money transition
5 service. Is that right?

6 A. That's, indeed, what the director of the-- what the FinCEN
7 person speaking has said, yes.

8 Q. Okay. Under the time circumstances, I'm going to say thank
9 you for your testimony.

10 MR. TOWNSEND: And unless there's a cross, we have
11 other witnesses we'd like the Court to hear.

12 MR. REYHANI: We'd like to reserve our right to recall
13 Mr. Gallancy at the conclusion of their examination.

14 THE COURT: Okay.

15 MR. REYHANI: Thank you.

DBLBBITH Hearing

1 UNITED STATES DISTRICT COURT
2 SOUTHERN DISTRICT OF NEW YORK

2 -----x

3 BITVESTMENT PARTNERS LLC,

4 Plaintiff,

5 v.

13 CV 7632 (RWS)

6 COINLAB, INC., CLI HOLDINGS,
7 INC., ALYDIAN INC., PETER
8 VESSENES and JOHN DOE,

8 Defendants.

9 -----x

New York, N.Y.
November 21, 2013
10:07 a.m.

12 Before:

13 HON. ROBERT W. SWEET,

14 District Judge

15 APPEARANCES

16 REYHANI NEMIROVSKY LLP
16 Attorneys for Plaintiff
17 BRYAN ISAAC REYHANI

18 LOEB & LOEB LLP
18 Attorneys for Plaintiff
19 DANIELLE JANINE KIWAK

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23 ROGER M. TOWNSEND

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16 MR. REYHANI: Yes, your Honor. We'd like to call
17 Mr. Gallancy.
18 THE COURT: Anything further from the defense?
19 MR. TOWNSEND: Nothing further, your Honor. Thank
20 you.
21 THE COURT: You're still under oath, Mr. Gallancy.
22 THE WITNESS: Yes, your Honor.
23 DANIEL GALLANCY,
24 called as a witness by the Plaintiff,
25 having been duly sworn, testified as follows:
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DBLBBITH Olsen - redirect

1 DIRECT EXAMINATION

2 BY MR. REYHANI:

3 Q. Good morning, Mr. Gallancy.

4 A. Good morning.

5 Q. Yesterday plaintiff's counsel-- excuse me, defense counsel
6 briefly touched on your qualifications as a chartered financial
7 analyst.

8 Would you be able to elaborate as to your educational
9 background?

10 A. Yes. I have a degree in physics and a degree in electrical
11 engineering.

12 Q. And where are those degrees from?

13 A. University of Pennsylvania.

14 Q. Do you have any graduate school degrees?

15 A. I have an MBA from Colombia Business School.

16 Q. And can you briefly describe for the Court your work
17 background?

18 A. Sure. I've been in the technology investing universe for
19 many years now, primarily working on-- or in large measure
20 working on investments in the semiconductor industry and
21 semiconductor capital equipment industry. And by that I mean
22 the companies that manufacture the machines that are used to
23 make semiconductors.

24 I've looked at lots of tech investments in my career.
25 And overall -- just number of investments overall, I've looked

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1 at hundreds.

2 Q. And you're familiar with all the terms that we've used
3 regarding 28-nanometer and 65-nanometer semiconductors or
4 chipsets?

5 A. Yes, both from my educational background and also from my
6 professional background. Very much so.

7 Q. Okay. And how far back does your experience with the
8 bitcoin industry go?

9 A. As far back as 2011.

10 Q. Is the fact that-- we've heard a lot about
11 impracticability.

12 Is the fact that bitcoin mining equipment is now
13 utilizing, or shortly in the future utilizing, 28-nanometer
14 technology some sort of surprise?

15 A. No. It's the most expected thing in the-- it's wholly
16 expected. It's exactly what one would expect.

17 Q. And why is it expected?

18 A. Because the ITRS roadmap that you had referred to before
19 basically talks about the progression of semiconductor
20 technology through time. And you have very large companies--
21 Intel, Samsung, Taiwan Semiconductor-- all basically
22 collaborating on sort of aggregated research and development
23 because they have to because of the inherent complexity and
24 size of the semiconductor industry makes it so that they have
25 to plan for many years in advance.

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1 So that's why that ITRS roadmap goes all the way out
2 to 2022 or something like that, because there's a ton of
3 advanced planning and people know many, many years in advance
4 what the technology node for semiconductors will be. It's not
5 a change in technology so much as just the regular course of
6 progress.

7 I think that Mr. Olsen referred to Moore's law and,
8 indeed, this is exactly it. It's just Moore's law and it's
9 widely known and widely expected.

10 Q. And this is rudimentary knowledge in the industry?

11 A. Yes.

12 Q. So if everyone knows that 28-nanometer chipsets are on the
13 horizon, why would anyone use 65-nanometer chips to mine for
14 bitcoins or for anything else?

15 A. Sixty-five-nanometer chips are still wholly viable for lots
16 of stuff. There's two things: First of all, it's a matter of
17 sufficiency. So it's just like if you have a computer that's a
18 year old, yes, you could describe it as obsolete, but it still
19 runs Microsoft Excel, it still runs Internet Explorer. It
20 still does everything you need to do. It's not the fastest in
21 the market, but you don't need the fastest or best on the
22 market to achieve the goal. You merely need something that's
23 sufficient to achieve the goal. And, indeed, 65-nanometer
24 chips do achieve the goal.

25 And as best as I understand, the vast majority of the
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1 equipment that is currently deployed in the bitcoin mining
2 network is not 28-nanometer equipment, but, in fact, equipment
3 that is further back. Now, you can't know for certain, but the
4 reason I say what I've said is because only very recently have
5 you seen the appearance of 28-nanometer equipment.

6 The other thing is, I should add, the proposition that
7 28-nanometer equipment is sort of the bee's knees doesn't make
8 that much sense. If you look at, like, the biggest foundry
9 company in the world, which is Taiwan Semiconductor, some 70 --
10 seven-zero -- percent of their revenue is from technology
11 that's -- air quotes here -- legacy, which is not 28 nanometer.
12 It's 45, 65, 110, et cetera, et cetera.

13 Q. But isn't it better-- essentially the defense has said that
14 they're unable to mine because they are facing all this
15 28-nanometer competition, more or less.

16 Isn't it better to mine with the 28-nanometer
17 chipsets?

18 A. Not necessarily. So that's the other thing that I think is
19 strange. It depends on a variety of factors. The first is
20 what you'd pay for that equipment. Right? And, also, the
21 price of bitcoins. It depends on a variety of variabilities
22 and a variety of inputs.

23 It's sort of like saying is it necessarily best to
24 buy the most advanced-- is it necessarily best to buy a brand
25 new car? Not necessarily. A used car will get you from Point

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1 A to Point B. It might not be as attractive on the road, but
2 it will still do the job. So it's really a matter of
3 sufficiency.

4 Q. Have there been any unexpected and/or disruptive changes in
5 technology in the bitcoin industry that will prevent bitcoin
6 mining from occurring?

7 A. No.

8 Q. Is the same algorithm in place, SHA-256, that has been in
9 place the entire time for the bitcoin protocol, if I'm phrasing
10 that correctly?

11 A. Yes. SHA-256 was contemplated from the very beginning. It
12 has been used from the very beginning. It was actually, from
13 my understanding, invented by the NSA several years ago and it
14 has been used in bitcoin mining since its inception in 2009.
15 And all of the chips -- be they 28 nanometer, 65 nanometer, 110
16 nanometer, regardless -- all run the same SHA-256 algorithm.
17 They all do the same thing.

18 THE COURT: What is the NFA?

19 THE WITNESS: I'm sorry, your Honor. The NSA,
20 National Security Agency.

21 THE COURT: Oh, NSA.

22 THE WITNESS: Sorry about that.

23 THE COURT: Good God, I hadn't realized we got them
24 into this.

25 MR. REYHANI: We got everyone involved.

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1 THE WITNESS: I'll try to keep them out. Sorry.

2 THE COURT: I should think.

3 Q. And that chip, the SHA chip, is what would run on this
4 stick that I presented to Mr. Olsen earlier. Correct?

5 A. Yes, for sure.

6 Q. Can any other algorithms besides SHA-256 be used for
7 bitcoin mining?

8 A. No.

9 Q. So if the same algorithm has been used, is it fair to say
10 that the technology behind bitcoin is exactly the same?

11 A. Yes.

12 Q. If you were given the task to mine bitcoins using your best
13 efforts, what would you do?

14 A. Well, there are a lot of options. The first thing I would
15 probably do, if I wanted to get it done pretty quickly, is I
16 would simply go out to the market and contract with third
17 parties. And you could do that very easily by, say, putting up
18 a website and saying I'm offering to pay you money to mine
19 bitcoins for me. And you could do that in, I don't know, a
20 couple of hours.

21 Q. How many miners would you guess exist?

22 A. Individual miners?

23 Q. Yes.

24 MR. TOWNSEND: Objection; calls for speculation.

25 THE COURT: Overruled.

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1 A. Thousands. Hundreds-- likely thousands.

2 Q. All right.

3 A. I can actually say it's actually not entirely speculative
4 because some of the order books for mining equipment companies
5 are sort of known on-line, on websites where people post their
6 orders. So it's likely in the thousands.

7 Q. Okay. Are you friendly with any miners?

8 A. Yes, I am.

9 Q. How do they go about their mining?

10 A. Multiple ways. One of them has both his own mining
11 equipment in his custody, in his possession, and he does it
12 sort of on site. And that person also has a host of mining
13 contracts as well. So he's done two different things and they
14 both work out nicely for him and he's actually quite
15 profitable.

16 Q. So he --

17 A. And he's one person, just one guy.

18 Q. So that one person, his on-site equipment, where does that
19 sit?

20 A. I believe in his office.

21 Q. All right. And you mentioned the contracted-out portion of
22 it. So he's paying a third-party miner to mine bitcoins for
23 him?

24 A. Yes.

25 Q. All right. To your knowledge, has Coinlab attempted to

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1 procure the services of any third-party miners to deliver
2 bitcoins to Bitvestment?

3 A. They've certainly not apprised me of anything like that,
4 no.

5 Q. Let's say Coinlab went out to the market and procured the
6 services of third-party miners. Would that enterprise be
7 profitable?

8 A. Well, you never know for sure. I say this putting my
9 analyst hat on for a second. You never know for sure what will
10 be profitable in advance. Nobody can know. But certainly
11 there are many miners who are profitable. There's some miners
12 who are not. It's like any sort of-- any set of businesses out
13 there. There are going to be players: Players who are less
14 profitable, players who are unprofitable.

15 But, yes, there's certainly a possibility to make a --
16 there's definitely a possibility to make a profit; otherwise,
17 the industry wouldn't exist.

18 Q. And as the price of bitcoin goes up, the chances of that
19 profitability increases. Correct?

20 A. Tremendously so. So the one factor that I feel like people
21 aren't talking about very much is-- and I don't regard it as a
22 bubble and I don't think Coinlab could regard it as a bubble
23 either, because their whole nature is being involved in bitcoin
24 systems. They believe in it as well.

25 Now that the price of bitcoin has gone up sixfold,

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1 some huge amount, that basically increases your revenue as a
2 miner that much. So actually there are very few businesses
3 that I can think of as an analyst where you have this amazing
4 opportunity for your revenue on a U.S. dollar basis to increase
5 7x, some enormous number. To the extent that bitcoin continues
6 to be adopted, that curve will continue.

7 Q. And would you agree with me to say that bitcoin mining is
8 still in its infancy?

9 A. Yeah.

10 Q. It's just now hitting the mainstream more or less?

11 A. I mean, I would say-- I think that's a fair statement, yes.

12 Q. All right. Yesterday the defendants showed a financial
13 analysis for making purchases of mining equipment or capacity
14 from three vendors.

15 Do you understand why Mr. Vessenes has concluded that
16 none of those purchases would be viable?

17 A. No, I don't understand that.

18 Q. Why are you unable to understand that?

19 A. Because, yes, I am a financial analyst and, yes, I partake
20 in that industry. But what I was shown yesterday wasn't really
21 a financial analysis. It wasn't the work of a-- it wasn't the
22 work product that a financial analyst would really put
23 together. It was really just a set of input numbers and
24 conclusions and there's nothing in between. It's as if you
25 were to give me just two numbers, the input and the output. I

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1 have no idea how you got there so I have no idea what the other
2 assumptions in the model are.

3 Anyone can make a model that shows a lack of
4 profitability just by plugging in whatever assumptions they
5 want. So it was really just a piece of paper with two numbers
6 on it.

7 Q. Are there other ways that Coinlab could go about achieving
8 its goal of mining bitcoins?

9 A. Yes, there are many ways. I mean, I could list some of
10 them for you. There are manufacturers of mining equipment,
11 both enterprise grade and what they would call retail grade,
12 although I think the lines are becoming blurred. I know of at
13 least eleven such manufacturers off the top of my head that I
14 looked at recently.

15 Q. Okay. And --

16 A. There are probably more than that.

17 Q. And aside from going out to such manufacturers and such
18 vendors, what are the other ways that Coinlab could go about
19 complying with the terms of the contract?

20 A. Coinlab could comply with the terms of the contract simply
21 by reaching out to other miners and saying, hey, I need you to
22 mine these bitcoins for me.

23 There's also hosted mining, which is one of the
24 things we discussed. You could link up with mining pool
25 operators, and mining pool operators get a cut of some of the

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1 proceeds. And that's one way to do it. There are lots and
2 lots of ways to go about it.

3 Q. And if Coinlab contracted with any of these hosted mining
4 services or any third party, would that require Mr. Vessenes or
5 Mr. Olsen to be out of the office, not being able to tend to
6 Alydian's matters?

7 A. No. They make a phone call or two or go on the internet.
8 No, it would require very, very little monitoring and effort.
9 They just basically have to pay the monthly bill.

10 Q. How many vendors-- yesterday the defense presented a
11 situation where they're talking about the risk of equipment
12 catching on fire.

13 Would the defendant be subject to such a risk if they
14 bought a hosted mining contract?

15 A. No. No, hosted mining is done off premises, so it wouldn't
16 be on Coinlab's premises. Coinlab would not be at risk of some
17 sort of fire.

18 Q. How many vendors about which you're aware offer a hosted
19 mining service?

20 A. Probably about half a dozen, but there might be more than
21 that.

22 Q. Yesterday Mr. Vessenes testified that he had no idea how
23 many bitcoins had been mined between the date of the issuance
24 of the TRO and his testimony yesterday afternoon.

25 Are you aware between the signing of the TRO and

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1 yesterday at noon how many bitcoins had been mined by bitcoin
2 miners?
3 A. Yes, 62,925.
4 Q. Okay. So approximately 63,000?
5 A. Yes, sir.
6 Q. Okay. And how do you know that?
7 A. It's publicly available knowledge that you can go on the
8 internet and figure out. We just look at the number of blocks
9 mined at the time of the signing of the TRO and then look at
10 the number of blocks mined at the time of yesterday at noon, is
11 what you said, and you'd subtract and multiply by 25 and that's
12 it. It's as simple as that.
13 Q. If Coinlab utilized efforts to go about entering into one
14 of these mining contracts or going to any other third party to
15 procure their services to mine bitcoins, in your opinion what's
16 the probability that they would have delivered any bitcoin to
17 you by now?
18 A. A hundred percent.
19 Q. And how do you know that?
20 A. If you contract with one of these outsourced mining
21 providers or if you contract with miners directly or if-- you
22 bring up contracting. You could say that Alydian could be a
23 subcontractor to Coinlab. You could use any subcontractor and
24 give them any money, they could provide bitcoins that day.
25 Within hours, I mean.

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- 1 Q. Since we've heard testimony that Coinlab itself doesn't
2 mine, if Coinlab contracted with Alydian to mine your bitcoins
3 consistent with whatever is necessary in the bankruptcy court
4 proceeding, wouldn't that be Coinlab contracting with a third
5 party to mine bitcoins for it?
- 6 A. Yes. That's exactly it. So to be clear on that, any
7 fulfillment-- the idea of contracting with a third party is not
8 sort of a new idea. The idea that if Coinlab were to use
9 Alydian as its miner, it would indeed be using it. It would be
10 an affiliated party, but a third party.
- 11 Q. I want to discuss the bubble that was mentioned earlier.
- 12 A. Actually, I didn't finish. I should have answered your
13 question more clearly. That's one way they could do it, or
14 Coinlab could also do it directly. They don't have to contract
15 with a third party. They have a choice. I didn't demand that
16 they do one or the other.
- 17 Q. All right. I want to talk about the bubble that was
18 mentioned earlier for a second and the increase in hash rate.
- 19 Could you explain how it affects returns versus the
20 change in price of a bitcoin?
- 21 A. Yes. So hash rate, of course, has increased. It's
22 increased basically consistently for the past several months.
23 That's for sure true. So that means that any particular
24 bitcoin miner will receive fewer bitcoins for the same amount
25 of computing power that they put in, just as Mr. Olsen

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1 testified.

2 But the flip side of that is if you wished to sell
3 those bitcoins, collect the U.S. dollars for selling them, you
4 would now have seven times the amount of U.S. dollars that you
5 had before and you could redeploy that into more mining
6 equipment or do whatever you wish with it. Or most businesses
7 look at themselves on a profitability basis on U.S. dollars or
8 some other sort of conventional currency, and in that case your
9 enterprise could be tremendously profitable.

10 Q. We spoke a little yesterday, Mr. Vessenes testified about
11 the risk of a cyber attack on the bitcoin network. If the
12 bitcoin network were attacked, would that be an issue in terms
13 of mining?

14 A. Yes, that would be basically the end of bitcoin. Depending
15 on the type of attack, could result in either the end of
16 bitcoin altogether or it could result in-- it would be very
17 bad. The scenarios painted, contemplated, would be
18 extraordinarily bad for bitcoin and, in many cases, completely
19 unrecoverable.

20 Q. How would such a cyber attack occur?

21 A. It's not that hard. All that's required is-- and we
22 touched upon this yesterday in terms of what the purpose of
23 mining -- one of the purposes of mining in terms of securing
24 the network. So an attacker that would have 51 percent or more
25 than 50 percent of mining capacity could launch just this sort

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1 of attack by putting all their capacity on-line at once and
2 that would enable them to do a couple of things: First of all,
3 it would enable them to basically steal bitcoins essentially;
4 or, if they really wanted to, if they were a malicious attacker
5 and wanted to destroy the system, they could basically do an
6 attack where they'd put all the computing power on line all at
7 once and then take it off-line and then basically do a bunch of
8 stuff to render bitcoin transactions unable to clear. So
9 basically destroying the ability of bitcoin transactions to get
10 confirmations.

11 Q. All right. How much would it cost to launch a cyber
12 attack?

13 A. So not that much money in the grand scheme of things.
14 Probably on the order of magnitude of \$20 million.

15 Q. Okay.

16 A. Something like that.

17 Q. So if a country like China, for example, wasn't really
18 happy with bitcoins being used in their country, they
19 themselves, as an example, could launch a cyber attack and
20 bring down the entire bitcoin network?

21 A. Yes. And China's a very interesting example because China
22 has significant capital controls, and one of the things that
23 one can do with bitcoin is get around those capital controls.
24 They probably aren't too thrilled about that and actually their
25 cost would probably be even lower because they could basically

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1 just order some government-sponsored entities to just do it.

2 Q. Yesterday Mr. Vessenenes equated a cyber attack on the
3 bitcoin network to be akin to a cyber attack on bringing down a
4 Visa or MasterCard, or words to that effect.

5 Is that true?

6 A. It's not the same thing. I mean, people try to obviously
7 hack into Visa or MasterCard all the time and it's a
8 recoverable situation, because Visa and MasterCard are
9 companies and they eventually solve the problem and fix it.
10 And they're dealing in U.S. dollars which are backed ultimately
11 by the U.S. government. If bitcoin were cyber attacked,
12 there's no way necessarily to recover. That's the end. It's
13 good-bye.

14 Q. And is this a known issue in the bitcoin network?

15 A. Yes. It was actually discussed in the original White Paper
16 that described the bitcoin protocol. So this 51 percent
17 attack, so to speak, is actually contemplated in that paper.
18 So it's a known issue.

19 Q. And have you had conversations about this potential issue
20 with the defendants?

21 A. I have.

22 Q. In particular, Mr. Vessenenes?

23 A. I have.

24 Q. And Mr. Vessenenes has made public statements regarding that
25 issue as well?

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1 A. Yes, at the bitcoin conference in May, the conference
2 sponsored by the Bitcoin Foundation through which Mr. Vessenes
3 is the former chairman, I believe. He was on a security panel
4 and he discussed precisely this issue of the potential for a 51
5 percent attack to happen. I think he described it as-- he
6 described it as totally doable.

7 Q. Are there others that agree with this potential risk?

8 A. Many others. On that panel, the one that sticks out is a
9 guy named Dan Kaminsky, who is kind of this famous --

10 MR. TOWNSEND: Objection, your Honor. Calls for
11 hearsay.

12 THE COURT: Overruled.

13 Q. You can answer.

14 A. This guy Dan Kaminsky, who's a famous security researcher,
15 and kind of very well known in the security community. And
16 his quote on that same panel is also on the same YouTube clip
17 is, quote -- I'm paraphrasing because I don't remember his
18 exact words -- but I don't expect the proof of work function
19 to last through the end of the year. So he was basically
20 saying that he would expect something massive to happen by the
21 end of 2013 unless-- I don't know what unless. But he was
22 extremely concerned and quite animated on the panel in
23 discussing this.

24 Q. Okay. If an attack occurred, what would happen to
25 bitcoin?

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- 1 A. There are a lot of scenarios, but one of the scenarios
2 that's pretty easy to envision is that bitcoin would
3 essentially be rendered completely useless. So bitcoin would
4 kind of just go away or be rendered obsolete or-- "obsolete" is
5 not really the right word. Be rendered inoperable. That would
6 be the end, kind of curtains, for bitcoin. And also curtains,
7 therefore, for bitcoin mining.
- 8 Q. Why did you on behalf originally of yourself and also Dalsa
9 Barbour/Bitvestment, why did you enter into a contract with
10 Coinlab to mine bitcoins?
- 11 A. Because Mr. Vessenes represented to me on multiple
12 occasions that he would be 90 -- nine-zero -- percent of
13 network capacity. He did this -- that was, in a sense, the
14 sales pitch.
- 15 Q. Did he say it once?
- 16 A. He said it multiple times. We had conversations about it
17 in which he said -- basically he talked about whether or not
18 he wanted to disclose it to the world or whether or not he
19 wanted to keep it a secret. He gave the analogy of, like,
20 South Africa developing nuclear weapons and then sort of just
21 disclosing it to the world and then that sort of makes it safer
22 to do. Yes, he said it multiple times.
- 23 Q. Okay.
- 24 A. And I believed him because it was not at the time at all--
25 it was not an undoable thing. It was entirely doable at the

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1 time.

2 Q. Okay. You'll recall from yesterday's testimony that we
3 discussed a couple of addresses where Coinlab's or Alydian's
4 bitcoins were held.

5 Do you recall listening to that?

6 A. Yes, sir.

7 Q. And do you recall defense counsel making a representation
8 to your prior counsel that there were two addresses that
9 Coinlab -- although it changed yesterday to Alydian -- held
10 bitcoins? Correct?

11 A. Yes, sir.

12 MR. TOWNSEND: Objection, your Honor. This is the
13 same testimony that the Court declined to enter into evidence
14 yesterday.

15 THE COURT: Overruled.

16 Q. For the sake of ease, one address that was represented to
17 you started with 18 and --

18 THE COURT: Well, no, these were in the settlement
19 discussions. Correct?

20 MR. TOWNSEND: Yes, your Honor.

21 THE WITNESS: No, sir.

22 MR. REYHANI: No.

23 THE COURT: Well, wait a minute, folks. What was the
24 context in which you had these conversations?

25 THE WITNESS: Your Honor, my contract entitled me to
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1 full audit rights of the defendant, so I requested information
2 regarding their bitcoin output in compliance with those audit
3 rights. I was provided with those two addresses in compliance
4 with that audit rights request.

5 THE COURT: When?

6 THE WITNESS: I don't remember the exact date, but --

7 THE COURT: Well, roughly.

8 THE WITNESS: I believe it was in October, sir.

9 THE COURT: Thank you.

10 MR. TOWNSEND: Your Honor, the piece of evidence that
11 we were referring to yesterday was specifically declined to be
12 entered with the Court because it was included in settlement
13 discussions. Your Honor rejected that and now we're going over
14 it again and it's the same communication.

15 MR. REYHANI: Mr. Vessenes testified about the two
16 addresses.

17 THE COURT: Overruled.

18 BY MR. REYHANI:

19 Q. So you'll recall that there was a representation that
20 Mr. Vessenes testified about the two addresses yesterday, that
21 were purportedly Alydian's addresses, that started with 18AQ
22 and the other one that started with 1G3C.

23 Do you recall that testimony?

24 A. Yes, sir. Those addresses were explained to me to be
25 Coinlab. Not Alydian, but Coinlab addresses.

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1 Q. Okay. And if you'll recall, in your affidavit you set
2 forth some information that was retrieved from the internet
3 that showed bitcoins being transferred out from 18AQ and 1G3C
4 into another account that was 12zZ.

5 A. Yes, sir.

6 Q. And all of this information is publicly available?

7 A. Yes. The nature of the bitcoin network enables you to
8 trace transactions from one account to the other just by
9 looking at a website. It's extremely easy to do and readily
10 publicly accessible.

11 Q. And you'll recall from those exhibits to your affidavit
12 that certain of those transfers occurred on October 29th?

13 A. Yes, sir.

14 Q. And do you recall that certain of those transfers occurred
15 at around 1630, in terms of time of day?

16 A. Yes, sir.

17 Q. And is 1630 New York or is it Greenwich Mean Time? Are you
18 aware?

19 A. I believe that to be Greenwich Mean Time.

20 Q. So that's about one o'clock in the afternoon, 1:30 in the
21 afternoon New York time?

22 A. I believe so, yes.

23 MR. REYHANI: May I approach?

24 THE COURT: Yes.

25 Q. Could you explain to the Court the document that I've

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1 presented to you?

2 A. Yes, sir. It shows the transaction-- shows the transaction
3 going into that-- that 12zZ address that you referred to for
4 10,000 bitcoins.

5 Q. Okay.

6 A. And it has --

7 Q. Let's discuss the website first. What is this document in
8 general?

9 A. It's a screenshot of a website called Blockchain.info,
10 which enables anyone to look at any bitcoin address around the
11 world, you know, whatever you want to do, and to see the
12 transactions that have occurred to and from that address.

13 Q. Okay. And in the middle I've highlighted to speed things
14 along. That 12zZ address is the same 12zZ address that
15 received the --

16 MR. TOWNSEND: Objection, your Honor. This hasn't
17 been entered into evidence.

18 THE COURT: True.

19 MR. REYHANI: I was planning on admitting it after he
20 testified about it. We would submit it now if your Honor would
21 indulge us.

22 MR. SANTORI: At which point we would voir dire the
23 witness and likely object because this is hearsay, your Honor.

24 THE COURT: Be my guest.

25 MR. SANTORI: Thank you.

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1 VOIR DIRE EXAMINATION
2 BY MR. SANTORI:
3 Q. Mr. Gallancy.
4 A. Yes?
5 Q. Did you create this document?
6 A. No, I did not.
7 Q. How did you get it?
8 A. My attorney printed it out and handed it to me.
9 Q. Oh, I see. So is this the product of your attorney's
10 research?
11 A. No. I told him the web address to go to based upon tracing
12 transactions to the Blockchain, which is a very readily doable
13 thing, as you know.
14 Q. Is this your website?
15 A. This is not my website. It's Roger-- I shouldn't say whose
16 website it is because I actually don't know whose website it
17 is.
18 Q. Are you in the business of running websites?
19 A. I actually have run websites, yes.
20 Q. Are you in the business of running this website?
21 A. No, I'm not in the business of running this website, but
22 this website contains information that's publicly and readily
23 available through the Blockchain, as you know. It's all very
24 readily known because the Blockchain is a public ledger. In
25 other words, you wouldn't have to use this website to obtain
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DBLBBITH Gallancy - direct

1 this information. The information is all available on Block
2 Explorer. It's all well known and publicly available.

3 MR. SANTORI: I'd have to object to this as hearsay
4 and not falling into any exception.

5 THE COURT: Overruled.

6 MR. REYHANI: Your Honor, we'd like to offer this into
7 evidence as Plaintiff's Exhibit 1.

8 THE COURT: It's admitted.

9 (Plaintiff's Exhibit 1 received)

10 BY MR. REYHANI:

11 Q. So we were discussing the 12zZ address.

12 Is the 12zZ address that's highlighted for you in the
13 middle of the page the same 12zZ address that accepted about a
14 thousand bitcoins from the two Coinlab addresses that was
15 discussed yesterday afternoon?

16 A. Yes. I don't remember the exact number of bitcoins that
17 were transferred, but, yes, that is the address.

18 Q. How many bitcoins are being transferred into that 12ZZ
19 address?

20 A. In this transaction that I'm shown, it's 10,000, or
21 10,000.00000001.

22 Q. Okay. We can go with 10,000.

23 And what is the time and date of such transfer?

24 A. It's October 29th at 1637, which I believe to be Greenwich
25 Mean Time.

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DBLBBITH Gallancy - direct

1 Q. So that 1637 -- which is about 1:30 in the afternoon
2 here -- is just a few minutes after the two transactions that
3 we were discussing yesterday. Correct?

4 A. Yes, sir.

5 Q. Okay. I'd like to show you another document, if I may. Is
6 this similar information from the same website?

7 A. Yes, sir.

8 Q. Okay. And here the address is the same 12zZ address that
9 we were discussing a moment ago?

10 A. Yes, sir.

11 Q. And how many total bitcoins are sitting in that address, if
12 you can tell?

13 A. 15,101.29024042.

14 Q. Okay.

15 MR. SANTORI: Your Honor, we have to enter the same
16 objection as before. He's just reading from a document that
17 hasn't been entered into evidence. I presume if Mr. Reyhani
18 wants to enter it into evidence, we would object on the same
19 grounds.

20 MR. REYHANI: We offer it into evidence, your Honor,
21 as Plaintiff's Exhibit 2.

22 MR. SANTORI: And we object on the same grounds as
23 before, that this is hearsay.

24 THE COURT: Overruled. It will be admitted.

25 (Plaintiff's Exhibit 2 received)

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1 BY MR. REYHANI:

2 Q. So there's 15,100 and change of bitcoins that are sitting
3 in the 12zZ account?

4 A. Yes, sir.

5 MR. REYHANI: Nothing further at this time.

6 THE COURT: Let me just ask you, is it your view
7 that-- what is the -- you mentioned 62,925. Is it your view
8 that that is what has been mined by Alydian?

9 THE WITNESS: No. No, your Honor.

10 THE COURT: What is that number?

11 THE WITNESS: That's the number of bitcoins that have
12 been mined globally.

13 THE COURT: Oh, okay. All right.

14 THE WITNESS: So --

15 THE COURT: So it is your position that somebody --
16 and you believe it to be, based on the testimony here, you
17 believe it to be Alydian -- has 15,000 bitcoins.

18 THE WITNESS: I believe it to be Coinlab, not Alydian.

19 But, yes, I do believe that they are in possession.

20 THE COURT: Okay. Thank you.

21 Anything?

22 MR. TOWNSEND: One moment, your Honor.

23 THE COURT: Sure.

24 THE WITNESS: Your Honor. Your Honor. I apologize
25 for the writing on the bottom of this. I didn't put that data.

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DBLBBITH Gallancy - direct

1 That's put in the Blockchain by --

2 MR. REYHANI: If I may actually have one more
3 question. I apologize.

4 THE COURT: Okay.

5 MR. REYHANI: My fault.

6 BY MR. REYHANI:

7 Q. So on Plaintiff's Exhibit 1, if I could turn your attention
8 back to that, that's the one that shows the 10,000 bitcoins
9 going into the 12zZ account?

10 A. Yes, sir.

11 Q. Underneath that, there's a public note. It says, "Hi. My
12 name is Preet Bharara and I'm a homeless Indian junkie. I'm
13 accepting donations to buy crack for me and my ugly wife.
14 Please help me. Thank you."

15 What is that?

16 A. So this is what I was trying to-- I didn't want to offend
17 the Court by showing him this, but this is information that is
18 embedded in the Blockchain likely by the defendant, as they are
19 the ones who sent these coins to this address. It's
20 basically-- you have this way of putting information into a
21 transaction beyond the transaction itself. And the information
22 that was put into this transaction is this public note, so to
23 speak.

24 Q. Okay. So irrespective of who actually inputted, somebody
25 had to affirmatively take the time to input this into the

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1 Blockchain?

2 A. Yes.

3 Q. And do most people know how-- do most miners know how to do
4 it or is there a different level of sophistication with regards
5 to it?

6 A. Well, basic miners who are kind of just mining for fun
7 probably aren't embedding things into the Blockchain. You have
8 to have a certain level of technical sophistication to embed a
9 message into a transaction. The regular bitcoin QT client that
10 is like the original client doesn't let you really do that
11 through the graphic user interface. You'd have to have a
12 certain level of technical savvy to make it happen.

13 Q. And none of the other transactions that we saw on either
14 one of the exhibits, Plaintiff's Exhibit 1 or 2, have that
15 note. Correct?

16 A. No, sir.

17 Q. Okay. Thank you.

18 MR. REYHANI: I have nothing further.

19 CROSS-EXAMINATION

20 BY MR. TOWNSEND:

21 Q. Mr. Gallancy, you testified earlier that you had a friend
22 or associate that currently provided a hosted service where you
23 could contract with them and they would mine bitcoins for you.
24 Right?

25 A. No, that is not actually what I said. What I said is I

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DBLBBITH Gallancy - cross

- 1 have a friend who is using such a service.
2 Q. Who's your friend?
3 A. His name is Ivan.
4 Q. Ivan? Can you spell hit last name?
5 A. Ivan Brightly. I believe it's B-r-i-g-h-t-l-y, I think.
6 Q. Who is he contracting with?
7 A. I believe KnCMiner.
8 Q. KnCMiner?
9 A. I believe so, yes. I'd have to ask him, but yes.
10 Q. When did he start doing that?
11 A. Fairly recently.
12 Q. Can you be more specific?
13 A. I didn't ask him the exact date, but it was fairly recent
14 because we were discussing it fairly recently and he wasn't
15 doing that before.
16 Q. Okay. So it was within the last week?
17 A. I don't think it was within the last week. It was probably
18 within the last-- I honestly don't know the specific date. My
19 suspicion is it's within the last two or three weeks, but I
20 don't know the specific dates, sir.
21 Q. Sure. And how much has he paid KnCMiner?
22 A. We didn't discuss the specific payment arrangements of his
23 transaction.
24 Q. So you don't know how much he's paid?
25 A. I don't know how much he's paid, but one can look it up on
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DBLBBITH Gallancy - cross

- 1 the internet because that sort of information is available. I
2 had a conversation with, long ago, the head of KnCMiner and you
3 could get him on the phone and negotiate deals with him.
4 Q. And who is the head of KnCMiner?
5 A. One of the guys is a guy named Sam Cole.
6 Q. Can you spell that?
7 A. I think it's just S-a-m C-o-l-e.
8 Q. Okay. And do you know how many bitcoins Mr. Brightly has
9 mined?
10 A. I don't know off the top of my head, sir, no.
11 Q. So you don't know whether he spent more than he received.
12 Right?
13 A. I don't know whether he spent more than he's received, but
14 I know that he engages in mining.
15 Q. Okay. And would you approve Coinlab spending money on KnC
16 in advance to go mine bitcoins?
17 A. Would I approve it?
18 Q. Yes, today.
19 A. Sure.
20 Q. And would you approve the capital and operational
21 expenditures to be paid for out of the bitcoins money?
22 A. Well, with the arrangement that you were just describing,
23 the host mining, there are no capital and operational
24 expenditures in that context. It's a mining contract where you
25 just pay like a -- I think it's a monthly fee or whatever it

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DBLBBITH Gallancy - cross

- 1 is. So --
2 Q. So it's free?
3 A. No, no. I just said you pay a monthly fee.
4 Q. Okay. And what if the costs, whatever they may be, are--
5 do you know-- you've testified that you don't know whether the
6 costs exceed or are less than the revenue associated with
7 that, but would you approve Coinlab spending money on KnC
8 without knowing whether it would be a net and a positive cash
9 flow?
10 A. I would in this instance for two reasons: Number one, the
11 whole idea behind Coinlab, if I understand, is that it's a
12 bitcoin incubator and, therefore, they continue to believe that
13 the price of bitcoin will go up and, therefore, even if the
14 bitcoins they receive today are only worth "X" dollars and if
15 that "X" dollars is below their cost for the mining, if you
16 were to hold on to those bitcoins, they would be worth a lot
17 more later on.
18 Q. So your belief is that Coinlab is long on bitcoins?
19 A. That's not what I said, no, sir.
20 Q. Is that your belief?
21 A. When you say "long on bitcoins," can you please explain?
22 Q. What does that mean to you, long on bitcoins, to be long on
23 an investment?
24 A. To be long an investment.
25 Q. Say that again.

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DBLBBITH Gallancy - cross

1 A. Okay, I understand. I think that's two separate
2 questions. I believe that Coinlab does, indeed, possess
3 bitcoins, yes, sir.

4 Q. Yes.

5 A. And I also do believe that Coinlab's business plan -- and
6 actually Mr. Vessenes had stated to me bitcoins' (sic) original
7 strategy, so to speak, is to have bitcoins and then work within
8 the ecosystem to encourage the value of those bitcoins to
9 increase.

10 Q. And, in fact, you believe that Coinlab has 15,000 bitcoins.
11 Correct?

12 A. I believe so --

13 Q. At least.

14 A. I believe so, yes.

15 Q. And you believe them to have that today. Is that right?

16 A. I believe so, yes.

17 Q. And you have no knowledge whether those bitcoins were the
18 result of mining or from a direct transaction or other
19 transfer. Is that right?

20 A. Well, I do have some knowledge of that because the input
21 transactions to that 15,000 included those two bitcoin
22 addresses that we were referring to earlier. And those are the
23 addresses at which you, sir, represented to me Coinlab is
24 mining.

25 Q. Right. But we refer to Coinlab generally as including all

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DBLBBITH Gallancy - cross

1 of the affiliated entities, don't we?

2 A. No, sir. In your letter to me, you didn't refer to Alydian
3 even once. You specifically referred to Coinlab. It was
4 specific.

5 Q. Right. But the testimony in court by the actual miners has
6 been that Coinlab hasn't engaged in any mining since, I think
7 it was 2012. Is that right?

8 A. Sir, I can't speak to other people's testimony, but --

9 Q. Well, you were here. Right?

10 A. I'm sorry?

11 Q. You were here. You observed that testimony. Right?

12 A. I was here, yes, sir.

13 Q. Okay. And you testified that someone could hack the
14 bitcoin mining network if they obtained 51 percent of all
15 bitcoin mining capacity. Is that right?

16 A. Yes. Actually recent computer science papers show that
17 it's likely doable with less than 51 percent.

18 Q. Right. But your testimony was 51 percent. Right?

19 A. Yes, sir.

20 Q. And how much does it cost to buy terahash capacity today?

21 A. It depends on how you purchase it and it depends on the
22 mechanism. I've seen costs sort of very overtly in the \$5,000
23 range. Those are sort of I guess what you guys would call
24 retail costs, but it's possible to purchase it likely for less
25 than that depending on the arrangements that you make with the

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DBLBBITH Gallancy - cross

- 1 provider.
2 Q. Well, would you disagree with the assessment that it costs
3 between \$30,000 and \$120,000 to buy a terahash today?
4 A. I'm sorry? That it would cost between \$30,000 and \$100,000
5 to buy a terahash?
6 Q. Correct.
7 A. Yes, I would disagree with that assessment.
8 Q. And if the network is-- assume for the sake of argument
9 that it cost \$30,000 to buy a terahash.
10 A. Wait.
11 Q. Just for the sake of argument.
12 A. Yes, sir.
13 Q. I understand your testimony is otherwise.
14 A. Yes, sir.
15 Q. And if you needed to buy 51 percent of the bitcoin mining
16 network to hack the network, wouldn't it cost-- again I'm going
17 to make you do math, just like I did Mr. Olsen-- and we're at
18 5,000 terahashes, so therefore you'd have to buy 2,501
19 terahashes times 30,000. Is that right?
20 A. If you were to use your 30-- actually I think your math is
21 in-- well, okay. If we use your 30,000 number, then that's the
22 number you're going to use. I think it's an order of magnitude
23 less than that. It's one-tenth that. But you're actually--
24 you're also actually underestimating the amount of capacity
25 you'd have to get. Because if the network's running at 5,000

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DBLBBITH Gallancy - cross

1 and you were to buy 2,500, that would only put you at a third.
2 So you'd have to gross it up. So there are a couple of
3 things wrong with that math, but I guess I get where you're
4 going.

5 Q. So many, many millions of dollars, right, under my
6 assumptions?

7 A. My estimate is there would be about 15 -- one-five --
8 million dollars. Fifteen, 20. Fifteen, 20, something along
9 those lines depending on how you do it.

10 Q. And you haven't provided any data or detailed financial
11 records which demonstrate that the cost of bitcoin mining would
12 exceed the revenues from bitcoin mining or--

13 A. I have not provided any evidence that the cost of bitcoin
14 mining would exceed the revenue from bitcoin mining.

15 Q. And you haven't provided any financial records
16 demonstrating that the revenue from bitcoin mining ventures
17 would exceed the cost of bitcoin mining. Is that right?

18 A. I have not provided such records. If asked to do so, I
19 would be happy to build a model.

20 Q. Right. Well, you know it's your burden of proof here
21 today. Right?

22 A. Is it my burden of proof?

23 MR. REYHANI: Objection; calls for a legal
24 conclusion.

25 THE COURT: Sustained.

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DBLBBITH Gallancy - cross

1 Q. And is it your position that you can direct Coinlab to
2 engage in a bitcoin mining enterprise where costs exceed the
3 revenue?

4 A. It is my position that Coinlab is obligated to mine for me
5 7,984-odd bitcoins.

6 Q. Right, less approved operational and capital expenditures.
7 Correct?

8 A. If approved by both parties, indeed so. If approved by
9 both parties.

10 Q. Right.

11 And so does that lead you to conclude that you can
12 compel under the contract for Coinlab to engage in a
13 money-losing enterprise?

14 A. I'm not asking Coinlab to do anything except for mine the
15 7,984 bitcoins.

16 Q. Right.

17 Can you answer that question, though, the question I
18 asked?

19 A. Ask it again, please.

20 Q. Do you believe under the contract that you can compel
21 Coinlab to engage in a business enterprise in which the costs
22 exceed the revenue?

23 A. If the costs exceed the revenue for Coinlab to mine the
24 7,984 bitcoins, that's unfortunate, but I believe that
25 ultimately they can achieve the goal of mining those

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DBLBBITH Gallancy - cross

1 bitcoins.

2 Q. Okay. You still haven't answered the question. Do you
3 believe-- and I'll ask it a third time.

4 Do you believe that you can compel Coinlab to engage
5 in a business enterprise in which the costs exceed the
6 revenues?

7 MR. REYHANI: Objection; asked and answered.

8 THE COURT: Overruled.

9 A. If the costs exceed the revenues for a time, then, yes. If
10 that's required in order to fulfill the contract, then, yes.
11 For a time that may be the case, just as for any start-up at
12 the time, in the beginning, the costs may exceed the revenues.
13 That happens with most start-ups.

14 Q. And what also happens with many start-ups, as Mr. Reyhani
15 elicited earlier, a lot of them fail. Right?

16 A. Many fail, yes.

17 Q. All right.

18 A. Many succeed as well.

19 Q. Right.

20 More fail than succeed, though, right, just like the
21 restaurant business?

22 A. More fail than succeed, yes.

23 Q. And you knew when you were investing in-- strike that.

24 You knew when you became a customer that you were
25 engaged in a speculative start-up. Is that right?

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DBLBBITH Gallancy - cross

- 1 A. No, sir. Actually, when I became a customer, I was not
2 engaging in a speculative start-up. I was a customer of what I
3 understood would be a well-capitalized business where the
4 defendant represented to me that he would be 90 percent of
5 network capacity and that he was backed by guys like Tim
6 Draper.
7 Q. But you knew there was a risk that the start-up would fail.
8 Right?
9 A. There's a risk that any business would fail, sir.
10 Q. Right.
11 I'd like to ask you about this kind of inflammatory
12 language in the bitcoin address.
13 I'd like to sort of avoid recalling another witness,
14 but do you really believe that this was the language of one of
15 the people in this courtroom?
16 A. I believe so.
17 Q. And upon what basis do you believe that?
18 A. The timing of the transaction and the transaction
19 destination.
20 Q. Okay. But I'm talking about this Indian situation.
21 A. Yes, that's what I'm talking about.
22 Q. Okay. And you don't believe that this can be just added
23 through a button on the Blockchain website?
24 A. I don't believe it can be added through a button on the
25 Blockchain website, no, sir.

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DBLBBITH Gallancy - cross

1 Q. All right. You testified yesterday that you believe that
2 you could sell 8,000 bitcoins in the bitcoin network today. Is
3 that right?

4 A. That I could sell 8,000 bitcoins in the bitcoin network?

5 Q. Or on a bitcoin exchange today. Right?

6 A. You could sell 8,000 bitcoins on a bitcoin exchange today,
7 yes, sir.

8 Q. Or you could transfer that to an individual third party for
9 currency today probably. Right?

10 A. If you so wished, yes, sir.

11 Q. Right.

12 A. Well, over-the-counter transactions of that size become
13 sort of cumbersome to do, but, hypothetically, yes.

14 Q. Right.

15 So if you were to ultimately prevail in this case and
16 establish that today you are entitled to 7,900 bitcoins, we
17 would be able to determine what the dollar value of those
18 bitcoins were today, couldn't we?

19 A. Changes minute by minute, but you could determine it at any
20 particular one second, yes, although there are some
21 complexities behind that because there are special things
22 that you could do with bitcoin that you can't do with regular
23 money.

24 Q. Right.

25 But you could turn them into money. Right?

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DBLBBITH Gallancy - cross

1 A. You can turn them into money, just as you could turn a car
2 into money by selling it, yes, sir.

3 Q. Right.

4 MR. TOWNSEND: One second, your Honor.

5 (Pause)

6 MR. TOWNSEND: Just one further question.

7 Q. This USB, did you purchase this?

8 A. I did, sir.

9 Q. And how much did you pay for it?

10 A. I believe it was \$35, maybe \$40.

11 Q. And when did you buy it?

12 A. A couple days ago.

13 Q. A couple days ago.

14 And how many terahashes would this give you on it?

15 A. It would give you less than a terahash.

16 Q. Could you be more specific?

17 A. I forget the exact technical specifications of it, but it
18 is less than a terahash, yes.

19 Q. And Mr. Olsen testified earlier regarding how many
20 terahashes. Did it sound like accurate testimony, .0002, I
21 believe it was?

22 A. I believe actually Mr. Olsen gave an estimate as to how
23 many bitcoins it would produce, not the number of terahashes
24 that the device provides.

25 Q. Okay.

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